

**Before the  
Federal Communications Commission  
Washington, D.C. 20554**

In the Matter of	)	
	)	
Developing a Unified Intercarrier	)	CC Docket No. 01-92
Compensation Regime	)	

**COMMENTS  
of the  
NATIONAL RURAL TELECOM ASSOCIATION  
and  
THE ORGANIZATION FOR THE PROMOTION AND  
ADVANCEMENT OF SMALL TELECOMMUNICATIONS COMPANIES**

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## SUMMARY

The Commission's Notice proceeds from an underlying premise that initial, interim intercarrier compensation reforms are in place for all carriers, and thus it may be time to explore longer-term solutions. However, that is not the situation for carriers operating under ROR regulation. Because ROR ILECs' existing access charge regime is in flux, it is too early for interested parties to evaluate, and the Commission to endorse or adopt, a long-term post-transition plan of any kind for these carriers. Proposing seismic changes in this proceeding, before the MAG proceeding has reached its conclusion, seriously undermines the regulatory stability ROR carriers seek and compounds the disincentive such uncertainty has on investment in advanced services infrastructure.

The proposals made in the NPRM have expansive potential repercussions as carriers' and end-users' responsibilities for bearing the costs of the nationwide public switched network are reallocated. Although the Commission has chosen to proceed by rulemaking, the drastic nature of the changes under consideration dictates that all affected parties receive an opportunity for full participation in identifying additional issues raised by a bill-and-keep regime or by any other reform measures.

Given the significant jurisdictional cost allocation and intrastate rate ramifications of a bill-and-keep regime, NRTA and OPASTCO agree with NARUC that the separations and universal service issues must be referred to the respective joint boards. In addition, the Commission should conduct its proceedings to involve any state that is interested in whether intrastate operations are to be part of a nationwide bill-and-keep requirement for all intercarrier compensation.

The Commission should make a careful assessment of the existence and pace of technological changes and their impacts on the current access charge regime. If market distortions caused by disparate regulations are not currently expanding at an explosive rate, then the Commission can avoid being stampeded into premature action.

As the Commission moves forward with its reform proposals, it is obligated to ensure -- prior to the adoption of any new regime -- that the universal service principles mandated by section 254(b) of the 1996 Act will continue to be met. This includes the directives that end-user rates remain affordable and that there be reasonable comparability between rural and urban rates and services. In addition, toll rates must remain geographically averaged and integrated, as required by section 254(g).

An intercarrier compensation regime in which market efficiency and facilitating competition were the only goals would be disastrous in rural areas where there is hardly a market, unless there were specific, effective mechanisms implemented concurrently to deal with the universal service impacts. Thus, if an intercarrier compensation regime is chosen in which efficiency is the primary goal, then it is essential for the Commission to take all steps necessary to preserve and advance universal service *before* it adopts a new system. If rural ILECs were unable to recover all of their costs under a new regime, it would certainly act as a disincentive to rural telephone companies' buildout of a broadband capable network.

The small and dispersed customer bases of rural ILECs are insufficient to allow these companies to recover their access and interconnection costs entirely from their end-users. Rural carriers' per-subscriber costs are significantly higher than for non-rural carriers and a higher percentage of those costs are presently recovered through access charges. Furthermore, smaller calling scopes require the customers of rural ILECs to make a greater number of toll calls. Thus,

without a sufficient support mechanism, a bill-and-keep regime that requires rural ILECs to recover all of their access and interconnection costs from their end-users could have serious implications for universal service and network usage.

A bill-and-keep regime would certainly make it more difficult for the Commission to preserve and advance universal service – and impossible if the USF remains capped. Under bill-and-keep, much of rural carriers’ costs of providing interstate access would be “de-averaged” and need to be recovered directly from high-cost end-users, absent an effective countervailing support mechanism. In addition, bill-and-keep would make the NECA access pools far less viable. If the Commission is unwilling to allow universal service funding to grow beyond the presently imposed cap, end-user charges and rates in many rural areas will almost certainly become unaffordable and/or incomparable to urban rates.

Finally, the Commission seeks to assess the extent to which increases in flat-rated charges may affect telephone penetration levels. NRTA and OPASTCO believe that even a small drop in subscriber penetration is unacceptable and entirely inconsistent with our nation’s universal service policy. The Commission must not approach the universal service implications of intercarrier compensation reform from the standpoint of how much burden subscribers are willing to endure for a virtual necessity. It should, instead, seek ways to maintain the same rate affordability and comparability high-cost customers now have, while still providing carriers with the resources to invest in and deploy new and advanced services.

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**COMMENTS OF NRTA AND OPASTCO**

**I. INTRODUCTION**

The National Rural Telecom Association (NRTA) and the Organization for the Promotion and Advancement of Small Telecommunications Companies (OPASTCO) hereby submit these joint comments in response to the Notice of Proposed Rulemaking in the above-captioned proceeding.<sup>1</sup> NRTA is an association of incumbent local exchange carriers (ILECs) that obtain financing under Rural Utilities Service (RUS) and Rural Telephone Bank (RTB) programs. OPASTCO is a trade association representing over 500 small ILECs serving rural areas of the United States. All of the members of both associations are rural telephone companies as defined in 47 U.S.C. §153(37).

The primary purpose of the Commission's Notice is to seek comment on the feasibility of a bill-and-keep approach for intercarrier compensation. This proposal has tremendous, far-reaching implications for the entire telecommunications industry and consumers nationwide. The Commission must proceed cautiously and provide ample opportunity for all industry stakeholders to identify and thoroughly analyze the myriad issues involved prior to making any significant changes in intercarrier compensation policy. For the rate of return (ROR)-regulated

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<sup>1</sup> Developing a Unified Intercarrier Compensation Regime, CC Docket No. 01-92, *Notice of Proposed Rulemaking*, FCC 01-132 (rel. April 27, 2001). (Notice, NPRM)

ILEC members of NRTA and OPASTCO, it is particularly difficult to analyze the impacts of a bill-and-keep proposal prior to the adoption of an interim access charge reform plan. Moreover, the universal service and end-user rate ramifications of a bill-and-keep regime have the potential to be especially acute in the high-cost territories of rural carriers, which must be accommodated before such a plan could ever be adopted in these service areas.

**II. BILL-AND-KEEP FOR INTERSTATE ACCESS CHARGES (SEC. III.B.9. OF NPRM) -- THE COMMISSION AND THE AFFECTED PARTIES CANNOT FULLY EVALUATE THE NPRM'S PROPOSED BILL-AND-KEEP REGIME OR ANY OTHER INTERCARRIER COMPENSATION CHANGES FOR RATE OF RETURN ILECS BEFORE THE COMMISSION ADOPTS A COMPREHENSIVE ACCESS REFORM PLAN**

In this proceeding, the Commission has begun “a fundamental re-examination of all currently regulated forms of intercarrier compensation,” seeking comment on (1) the feasibility of a unified bill-and-keep regime for all intercarrier payment flows, (2) modifications to existing intercarrier compensation regimes, and (3) other possible intercarrier compensation approaches.<sup>2</sup> The Commission’s purpose is “to move forward from the transitional intercarrier compensation regimes to a more permanent regime that consummates the pro-competitive vision of the Telecommunications Act of 1996 ....”<sup>3</sup>

The NPRM proceeds from an underlying premise that initial, interim reforms are in place for all carriers, and thus it may be time to explore longer-term solutions. That premise may make sense for much of the telecommunications industry. However, that is not the situation for carriers operating under ROR regulation. Consequently, it is too early in their reform process to jump ahead to post-transitional analysis and long-term changes. The Commission points out that it has established interim intercarrier compensation measures for competitive local exchange

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<sup>2</sup> NPRM at paras. 1, 129.

<sup>3</sup> *Ibid.* at para. 1.

carriers (CLECs) and traffic bound for Internet service providers (ISPs).<sup>4</sup> It reports that the five-year transitional Coalition for Affordable Local and Long Distance Service (CALLS) reforms for price cap-regulated ILECs are in place.<sup>5</sup> Thus, these transitional arrangements can be evaluated. However, the Commission is considering, but has not yet adopted, a “transitional regime” for ROR ILECs in the Multi-Association Group (MAG) proceeding.<sup>6</sup> Thus, the Commission has no transitional or interim plan in place for ROR ILECs that can provide the basis for impact determinations here. Nor is there a reason to pursue the Commission’s announced purpose of obtaining “comment on the broad universe of existing intercarrier arrangements”<sup>7</sup> for ROR carriers, since their “existing arrangements” are already under review and will almost certainly *not* be the same “existing intercarrier regime” that the Commission will need to look at when the proper time comes for developing a longer-term solution.

Because the existing access regime for ROR ILECs is in flux and will change while this proceeding is underway, and a transition plan has yet to be put into effect, it is plainly too early to evaluate the effects of a bill-and-keep plan or other post-transition, long-range changes. Until the MAG plan (or a similar five-year plan) has been put into place, neither the Commission, ROR ILECs, their customers, nor any other interested party can reasonably analyze -- let alone endorse or adopt -- a long-term, post-transition plan of any kind. The inability to gauge the impacts on ROR carriers and their customers is particularly adverse when the Commission is considering a plan involving drastic changes from the cost recovery requirements and arrangements that have governed incumbents in the past. The Commission should refrain from

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<sup>4</sup> *Id.* at para. 3.

<sup>5</sup> *Id.* at para. 97.

<sup>6</sup> See Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers, CC Docket No. 00-256, *Notice of Proposed Rulemaking*, FCC 00-448 (rel. Jan. 5, 2001).

<sup>7</sup> NPRM at para. 2.

producing a sequel to the five-year plan it will adopt in the MAG proceeding, when the MAG episode is still in production.

One of the pivotal purposes of the MAG plan and the Commission's resulting rulemaking proceeding to adopt a five-year interim plan for ROR ILECs is to bring greater regulatory certainty to ROR carriers. The certainty of a five-year plan is essential because regulatory uncertainty is an obstacle to rural infrastructure development, and broadband deployment is a national priority. Proposing unprecedented changes in this proceeding before the MAG proceeding has even reached its conclusion seriously undermines the stable environment that the Commission and the ROR carriers are trying to create. Indeed, uncertainty about whether further investments in broadband can be recovered has already taken a toll on small and midsize ILECs' willingness to invest. This chilling effect can only be compounded by premature consideration of what will come *after* the supposedly stable five-year interim period, once it is in place.

Until the Commission acts on the MAG plan or other comprehensive five-year plan, the ROR carriers are at a disadvantage in comparison to the remainder of the telecommunications industry. This industry segment generally has the least regulatory flexibility to respond to competition and the least information about how they will recover their costs in the future -- even in the short term. ROR ILECs are also alone in that this Commission has not yet provided them with a feasible incentive regulation option.<sup>8</sup>

As NRTA and OPASTCO demonstrate below, there are also many major unknowns about the impacts, implications, and risks of a unified bill-and-keep approach for all intercarrier compensation that must be evaluated and suitably resolved before the Commission could responsibly adopt such a plan. There are questions to be answered with regard to all ILECs, to

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<sup>8</sup> Indeed, the adoption of the CALLS plan has, in effect, removed even that regulatory choice for ROR carriers.

be sure. However, NRTA and OPASTCO submit that there are more potential adverse consequences for small and rural ROR carriers that will demand answers. Nevertheless, in the event that the Commission decides to move forward with a bill-and-keep experiment, NRTA and OPASTCO strongly urge against applying it to ROR ILECs until it has been tried and evaluated for larger carriers and within more economically self-sufficient markets. Indeed, one of the unknowns that the Commission needs to explore and resolve at an early point in its proceeding is how (or possibly whether) it can adopt bill-and-keep on a bifurcated basis, so that the impacts of the regime can be known before it is imposed on the high-cost, low-density areas served by small and midsize ROR ILECs. The Commission owes a complete evaluation, based on a known, stable interim regime capable of supporting adequate analysis and impact predictions, to rural customers in markets where service is harder to establish, sustain, and improve.

**III. GIVEN THE MAGNITUDE OF THE CHANGES PROPOSED IN THE NPRM, THE COMMISSION AND PARTIES MUST PAINSTAKINGLY AND THOROUGHLY IDENTIFY, ANALYZE, AND RESOLVE THE MANY ISSUES RAISED BY MOVING TO A BILL-AND-KEEP REGIME, PARTICULARLY FOR RURAL CARRIERS**

**A. The Commission Needs the Participation of the States and All Affected Parties to Identify the Information Necessary for Evaluation and Impacts of Any Bill-and-Keep Regime**

The Commission has taken on an enormous task in considering fundamental changes to the patchwork of arrangements and requirements for intercarrier compensation. These proposals have expansive potential repercussions as carriers' and end users' responsibilities for bearing the costs of the nationwide public switched network are reallocated. Although the Commission has chosen to proceed by rulemaking, rather than by Notice of Inquiry, and has identified many issues in the NPRM, the drastic nature of the changes under consideration dictates that affected

parties need an opportunity for full participation in “spotting” additional issues, questions, and concerns raised by either a bill-and-keep regime or by other reform measures.<sup>9</sup>

NRTA and OPASTCO agree with the National Association of Regulatory Utilities Commissioners (NARUC)<sup>10</sup> that the NPRM involves many unknowns that need to be “fully investigated by both the federal and state regulators,” ranging from the impacts on end-users, universal service, and states, to the creation of perverse infrastructure deployment incentives. In addition to the types of questions raised by NARUC, there are many concerns about the impacts specifically on rural telephone companies and their customers that require solutions before a new regime can be adopted. NRTA and OPASTCO discuss the universal service issues and impacts in more detail below in section IV. Examples of some of the questions raised by the Commission’s proposals are:

- The effect of a bill-and-keep regime on the utility and sustainability of the National Exchange Carrier Association (NECA) interstate access revenue pools and tariffs and any joint intrastate pools and tariffs. Moving to a bill-and-keep system may directly or indirectly destroy pooling, upon which most ROR carriers rely to avoid administrative burdens and share risks.
- The disadvantage of a system meant to encourage efficient negotiated arrangements for smaller carriers that lack leverage and may not even be able to persuade larger carriers to bargain with them in the first place.
- The impact of a bill-and-keep regime on the identity and responsibility of the carrier of last resort for interstate and intrastate services.

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<sup>9</sup> The Commission’s suggestion (NPRM at para. 99) that efforts to reform the existing calling-party’s-network-pays carrier compensation regimes should start with a prescription of a forward looking economic cost (FLEC) methodology means that *all* identified alternatives for long-term intercarrier compensation in the NPRM involve major changes, particularly for rural carriers. Rural carriers are not subject to the Commission’s Synthesis Model used for Universal Service purposes by non-rural ILECs and are generally exempt from FLEC-based ILEC local interconnection arrangements under section 251(f)(1) of the 1996 Act. Moreover, the Rural Task Force recently found the Commission’s existing FLEC cost model unsuited for the vastly varied universe of rural ILECs. *See* Rural Task Force Recommendation to the Federal-State Joint Board on Universal Service (rel. Sept. 29, 2000), p. 20.

<sup>10</sup> NARUC, Resolution Regarding the Development of a Unified “Bill-and-Keep” Intercarrier Compensation Regime (adopted July 18, 2001).

- The relative impacts of bill-and-keep on high-cost and low-cost ILECs and their customers, on residential and business customers, and on the comparability and pace of advanced services development in urban and rural markets.
- Whether incumbent carriers will get the pricing and regulatory flexibility needed to implement a bill-and-keep regime.
- Impact on the availability and cost of tandem switching and transport facilities to deliver traffic to the new required points of interconnection for small and rural ILECs under a bill-and-keep regime. The Commission's assumption that there will be significant competition to provide transport is not tenable for rural carriers' serving areas, which may leave them with exorbitant costs or no facilities.
- Impact on extended area service (EAS) arrangements and toll vs. local calling areas.
- Impact of arbitrage incentives and opportunities if only interstate bill-and-keep is adopted because of limitations on the Commission's authority.

These and the universal service concerns discussed in Section IV below, are examples of issues that must be resolved as a pre-condition to moving to a bill-and-keep system for rural ILECs. In addition, the NARUC resolution raises state concerns. NRTA and OPASTCO expect that CLECs, ISPs, and consumer representatives will identify their own lists of concerns that will need to be resolved. Our point is not that the Commission should refrain from moving towards a bill-and-keep system or other major reforms, but that a major task lies ahead to identify, consider, and resolve the many unknowns that are inevitable with far-reaching changes such as those proposed in the NPRM. NRTA and OPASTCO look forward to working with the Commission as it tackles the challenges of this proceeding.

**B. Legal Authority / Jurisdictional Responsibility (Sec. III.D.1.&2. of NPRM) -- Before Adopting a Unified Bill-and-Keep Regime, the Commission Must Refer the Intrastate and Universal Service Issues to the Appropriate Joint Boards and Obtain the Input of Individual States**

NARUC's resolution correctly points to the Commission's intention to include intrastate intercarrier compensation within the proposed bill-and-keep regime. NRTA and OPASTCO agree with NARUC that the separations and universal service issues must be referred to the

appropriate existing joint boards. There can be no question that the Commission's consideration of an inter- and intrastate bill-and-keep regime has significant jurisdictional cost allocation and intrastate rate ramifications. Sections 410(c) and 254(a) of the Communications Act of 1934, as amended, provide for the use of mandatory joint board proceedings on both separations and universal service issues.

However, the scope of the intrastate laws, rules, policies, authority, costs, rates, and services that the NPRM would affect go far beyond the issues that sections 410(c) and 254(a) contemplate. Instead, the adoption of a trans-jurisdictional bill-and-keep regime is more akin to the kind of conferences and joint hearings "regarding the relationship between rate structures, accounts, charges, practices, classifications, and regulations of carriers subject to the jurisdiction of such state commission and of the Commission" contemplated by section 410(b). That section does not give the Commission final authority, but should involve federal-state comity and consensus. Thus, while the two existing joint boards have an important and mandatory role to play on separations and universal service issues, they do not eliminate the Commission's responsibility not to impinge on state authority.

Therefore, in addition to the two joint board referrals requested by NARUC, the Commission should conduct its proceedings to involve any state that is interested in whether intrastate operations are to be part of a nationwide bill-and-keep requirement for all intercarrier compensation. The Commission may need to seek changes in the Communications Act of 1934, as amended, since the 1996 amendments in sections 251 and 252 specifically provide for a different intercarrier compensation structure and state role than what the NPRM has in mind. The current lack of consensus among states will make it exceedingly difficult to adopt a unified inter-

and intrastate bill-and-keep regime and adds to the Commission's challenge in moving toward its new intercarrier compensation paradigm.

Even if the Commission seeks to avoid conflict with the states by adopting an interstate-only bill-and-keep plan, the states will face arbitrage and other problems that will pressure the state commissions to mimic the interstate scheme. For example, toll carriers would have an incentive to make intrastate toll calls appear to be interstate in order to avoid access charges. This danger may provide further impetus for states to oppose the proposals in the NPRM.

**C. Before Adopting a Bill-and-Keep Regime, Especially for Rural Carriers, the Commission Needs to Analyze the Status and Impacts of Technology Changes on the Current Access Charge Regime in Order to Avoid Premature Intervention**

A key impetus for the Commission in opening this proceeding are the distortions that occur under current regulatory schemes when carriers take advantage of arbitrage opportunities inherent in applying different compensation regimes to entities providing essentially the same functions or services. One example recognized in the NPRM is that charging interexchange carriers (IXCs) access charges for long distance calls, while exempting ISPs, "gives the provider of IP telephony an artificial cost advantage over providers of traditional long-distance service."<sup>11</sup> Some also expect service and pricing breakthroughs as satellite and "3G" wireless networks become capable of delivering high-speed digital services and the use of cable broadband continues to increase. Others anticipate speedy digitalization of the nation's network and rapid substitution of packet switching.

It is true that technology is developing rapidly and that anomalies in regulation threaten distortions and encourage inefficient choices. It is also true that the Commission should not allow its rules and policies to favor or disadvantage particular technologies. However, the

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<sup>11</sup> NPRM at para. 12.

sweeping changes the NPRM proposes must not be hastily adopted, without adequate information and analysis, on the basis of presumptions about future developments and impacts. NRTA and OPASTCO urge the Commission to make a careful assessment of the existence and pace of technological changes and their impacts on the current access charge regime. To the extent that fact-finding shows that some distortions -- such as extensive migration to IP telephony to take advantage of the arbitrage opportunities that make Internet long-distance calls appear to be “free” -- are not currently expanding explosively, the Commission can avoid being stampeded into premature, inadequately-considered action.<sup>12</sup> The Commission can best make the right choices about long-term policies for intercarrier compensation by moving at a measured and careful pace rather than by succumbing to the panic that may be expressed by some industry participants.

#### **IV. BEFORE IT ADOPTS ANY NEW INTERCARRIER COMPENSATION REGIME, THE COMMISSION MUST CAREFULLY ANALYZE THE UNIVERSAL SERVICE IMPACTS AND TAKE ALL STEPS NECESSARY TO COMPLY WITH THE LAW**

Section 254 of the Telecommunications Act of 1996 sets out a series of universal service mandates and principles that the Commission must adhere to and that Congress held in equal importance to the competitive provisions of the Act. Two of those principles state that end-user rates should remain affordable, and that there should be reasonable comparability between rural and urban rates and services.<sup>13</sup> These two principles are separate and distinct. For example, even if the Commission determined that rates in rural areas will remain affordable after adoption

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<sup>12</sup> Certainly, the FCC should not hastily adopt an entirely new intercarrier compensation regime simply because it conveniently solves the arbitrage opportunity created by its own policy decision to exempt enhanced service providers from paying interstate access charges.

<sup>13</sup> “Quality services should be available at just, reasonable, and affordable rates.” 47 U.S.C. §254(b)(1).

“Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban

of a new intercarrier compensation regime, the universal service principles would not be fulfilled if rural services and rates are not also reasonably comparable to those available in urban areas.<sup>14</sup> In addition, section 254(g) requires rates charged by IXC's in rural and high-cost areas to be no higher than those charged in urban areas and that the interexchange rates charged in each state are no higher than the rates charged in any other state. The Commission must not abandon these, nor any other of the universal service mandates set forth in the 1996 Act, as it moves forward to reform the intercarrier compensation rules.

**A. Appropriate Goals for Intercarrier Compensation Rules in Competitive Markets (Sec. III.A. of NPRM) – Universal Service Must Continue to be a Paramount Concern in the Areas Served by Rural ILECs as the Commission Moves Forward with Reform of the Intercarrier Compensation Rules**

Following the lead of the Office of Plans and Policy (OPP) working papers Nos. 33 and 34, the NPRM suggests that in light of the competitive goals of the 1996 Act and the mandate that universal service support be explicit, intercarrier compensation rules can no longer achieve multiple goals. The NPRM suggests that efficiency should be the sole or paramount goal of intercarrier compensation policy.<sup>15</sup> More specifically, the authors of the working papers believe that an intercarrier compensation regime must “efficiently” allocate interconnection costs between carriers, which they contend will, in turn, lead to: the “efficient” use of the network by consumers, the “efficient” deployment of facilities by carriers, and the “efficient” development

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areas and that are available at rates that are reasonably comparable to rates charged in urban areas.” 47 U.S.C. §254(b)(3).

<sup>14</sup> In *Qwest Corp. v. FCC*, the 10<sup>th</sup> Cir. Ct. of Appeals determined that the Commission’s definitions for the statutory terms “reasonably comparable” and “sufficient” in the Ninth Report and Order and Eighteenth Order on Reconsideration in CC Docket No. 96-45 (14 FCC Rcd 20432 (1999)) were inadequate. On remand, the Court required the FCC to define these terms more precisely in a way that can be reasonably related to the statutory principles, and then to assess whether its funding mechanism will be sufficient for the principle of making rural and urban rates reasonably comparable. *Qwest Corporation v. FCC*, No. 99-9546 (10<sup>th</sup> Cir. 2001).

<sup>15</sup> NPRM at paras. 32, 33; *see also*, Patrick DeGraba, *Bill and Keep at the Central Office as the Efficient Interconnection Regime* at p. 15, para. 47 (Federal Communications Commission, OPP Working Paper No. 33, Dec. 2000); Jay M. Atkinson & Christopher C. Barnekov, *A Competitively Neutral Approach to Network Interconnection* at p. 3, paras. 6, 7 (Federal Communications Commission, OPP Working Paper No. 34, Dec. 2000).

of competition. While this may or may not be true, if an intercarrier compensation system is chosen in which efficiency is the primary goal, it is essential for the Commission to analyze the universal service impacts of that system carefully and take all steps necessary to preserve and advance universal service *before* it adopts a new system. Otherwise, rural subscribers may be “efficiently” left behind because market forces alone will not satisfy section 254.

As the carriers of last resort in their service areas -- and most often the *only* carriers providing ubiquitous service -- it is essential that rural ILECs be able to recover their costs, but in a way that does not make service second class or rates unaffordable for subscribers. The high-cost structure of serving sparsely populated markets has generally discouraged investment in rural telephony. However, the present mix of access charges, end-user charges, and universal service has made it possible for small and rural ILECs to make the substantial investments necessary to serve the most sparsely populated areas and to promote high subscriber penetration. Were the Commission to adopt an intercarrier compensation regime without ensuring full cost recovery and addressing the end-user rate implications, it is possible that the most “efficient” decision regarding infrastructure deployment in some high-cost, sparsely populated rural areas would be not to deploy. And, with all of the costs of access and interconnection shifted to end-users, the most “efficient” use of the network by high-cost rural consumers may be not to connect or not to use the network. These outcomes are antithetical to our Nation’s universal service policies and principles.<sup>16</sup>

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<sup>16</sup> The purpose of telecommunications policy is “...to make available, so far as possible, to all the people of the United States...a rapid, efficient, Nation-wide and world-wide wire and radio communication service with adequate facilities at reasonable charges...” 47 U.S.C. §151.

In other words, an intercarrier compensation regime in which market efficiency and facilitating competition were the only goals would be disastrous in rural areas where there is hardly a market, unless there were specific, effective mechanisms implemented concurrently to deal with the universal service impacts. Due to factors such as low population density, difficult terrain, and a lack of economies of scale, rural ILECs have significantly higher investments and operating expenses per subscriber compared to their non-rural carrier counterparts.<sup>17</sup> In addition, rural carriers, owing in part to smaller calling scopes, recover a far greater portion of their revenues through inter- and intrastate access than large ILECs. In fact, at this time, most small and rural ILECs derive, in aggregate, over 60 percent of their revenues through a combination of inter- and intrastate toll access charges and universal service support mechanisms.<sup>18</sup> In the 1996 Act, Congress recognized the starkly different operating environments of rural ILECs and the potential for harm to rural subscribers from purely market-based policies when it tempered its Sec. 251 market-opening requirements with a “rural exemption.”<sup>19</sup> The Commission must also acknowledge and address the unique market conditions of rural ILECs if it decides to move forward with an intercarrier compensation regime that is geared solely to achieving “efficiency.”

With regard to additional goals for any new intercarrier compensation rules, the Commission asks if it should consider whether a particular pricing regime encourages the efficient investment in, and deployment of, network infrastructure, including investment in

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<sup>17</sup> On average, total plant investment per loop is over \$5,000 for rural carriers compared to less than \$3,000 for non-rural carriers. On average, annual plant specific expenses per loop are \$180 for rural carriers compared to \$97 per loop per year for non-rural carriers. See Rural Task Force (RTF) White Paper 2, *The Rural Difference* (Jan. 2000) at pp. 12, 47, 54.

<sup>18</sup> The Commission itself has acknowledged that “some rate-of-return LECs receive more than 50 percent of their total revenues from interstate access and universal service support, compared to just over 25 percent for LECs subject to price cap regulation.” See Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation, CC Docket No. 98-77, *Notice of Proposed Rulemaking*, 13 FCC Rcd 14244 (1998).

<sup>19</sup> 47 U.S.C. §251(f).

broadband infrastructure.<sup>20</sup> If rural ILECs were unable to recover all of their costs under a new regime, it would certainly act as a disincentive to network investment, and stymie rural telephone companies' buildout of a broadband-capable network. This result would be at odds with the 1996 Act's overriding purpose of "accelerat[ing] rapidly private sector deployment of advanced telecommunications and information technologies and services to all Americans..."<sup>21</sup> It would also run afoul of the Act's universal service principles of access to advanced services in all regions of the Nation and access to advanced services in rural, insular, and high-cost areas that are reasonably comparable to those provided in urban areas.<sup>22</sup>

Just as important, the availability of advanced telecommunications services is both a catalyst for economic growth and a major enabling factor in the development of small business and manufacturing enterprises in rural areas.<sup>23</sup> In many instances, small ILECs receive a large portion of their revenue from one, or just a few, multi-line businesses in their territory. The loss of one of these business customers, in addition to being detrimental to the economic vitality of the community, would jeopardize the source of revenues that cover a portion of the cost of providing service to low-volume residential users. To ensure the continued provision of high quality service at reasonable rates and to encourage continued investment in advanced services in rural areas, intercarrier compensation policy cannot threaten to strand investments in rural ILEC networks which, in many cases, are the only networks providing or planning to provide advanced services in their territories.

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<sup>20</sup> NPRM at para. 33.

<sup>21</sup> Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56.

<sup>22</sup> 47 U.S.C. §254(b)(2), (3).

<sup>23</sup> Daryl J. Hobbs and Vicki M. Hobbs, *Rural America: Connections to the Future, Assessing the Extent of and Demand for Telecommunications Infrastructure in Rural America* at pp. 39-43 (OPASTCO White Paper, Nov. 1998).

**B. Impact on End-User Prices and Universal Service (Sec. III.D.3. of NPRM) – Without the Concurrent Provision of Additional High-Cost Support or Other “Cost Sharing” Mechanisms, a Bill-and-Keep Regime Could Have Devastating and Unlawful Consequences for End-User Prices and Universal Service in the Service Areas of Rural ILECs**

The small and dispersed customer bases of rural ILECs are insufficient to allow these companies to recover their access and interconnection costs entirely from their end-users. As explained, *supra*, the per-subscriber costs in rural ILEC service areas are significantly higher than for non-rural carriers, and a much higher percentage of those costs are recovered through access charges. In addition, subscribers of rural ILECs need to make a greater number of toll calls than do customers of non-rural carriers as a result of smaller calling scopes.<sup>24</sup> Thus, without a sufficient support mechanism, a bill-and-keep regime that requires rural ILECs to recover all of their access and interconnection costs from their end-user subscribers could have serious implications for universal service and network usage.

To begin with, there would be rate shock as a substantially greater portion of the high costs of rural networks would be recovered through those small subscriber bases. If those rates are too high, some subscribers could be forced to disconnect from the network. At the very least, network usage may be suppressed if the origination and termination charges imposed on end-users are too high. Furthermore, as previously noted, high end-user rates could cause the few “anchor” businesses located in rural service areas to relocate, causing residential rates to increase even further.

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<sup>24</sup> A comparison of the average local and toll revenue sources between rural and non-rural carriers shows that 66 percent of the average rural carrier subscriber’s bill comes from toll charges compared to only 53 percent for the average non-rural carrier customer. RTF White Paper 2 at p. 42.

Congress recognized when it adopted section 254(g) of the 1996 Act that it would be inconsistent with universal service principles if rural subscribers had to bear the higher cost IXC's incur in providing interexchange service to rural, insular, and other high-cost areas. It therefore mandated that these costs be averaged and integrated with the lower costs of serving urban areas, so that rural subscribers would be charged the same long distance rates as their urban counterparts nationwide. Under a bill-and-keep regime, however, much of rural carriers' costs of providing interstate access that were previously averaged nationwide by the IXC's in their rates would now be "de-averaged." This means these costs would need to be recovered directly from high-cost rural end-users, absent an effective countervailing support mechanism. Shifting the burden of high-cost service to end-users is contrary to the nationwide cost-sharing concept of section 254(g) and universal service generally.

In addition, a nationwide bill-and-keep regime should lead to a large reduction in toll rates, making it even more difficult for IXC's to financially justify serving low-volume toll users and subscribers in high-cost areas. If the major IXC's -- and in particular, AT&T -- stopped serving the areas served by rural ILECs, nationwide geographic toll rate averaging would cease to exist. It would also eliminate rate integration, which would have an adverse impact on Alaska, Hawaii, and other remote and insular areas. If this were to occur, a question would arise as to how these consumers would receive interstate toll service.

A bill-and-keep regime would also make the interstate access revenue pools administered by NECA far less viable. By participating in the NECA pools, member companies eliminate the need to file individual access charge tariffs and reduce the risk of volatility of individual company revenues. If the costs of access were passed on to end-users in the form of flat-rated

charges, it is doubtful that any carrier would agree to adopt a pooled end-user rate if it could justify a lower amount based on cost. This would initiate a death spiral for the pools, where an initial group of carriers exit the pool, the pooled rate rises, then the next group of lower-cost carriers exit, and so on until the pool ceases to exist. This is another illustration of how important cost sharing is to the preservation of universal service, even when it is just among the small, rural carriers.

The “de-averaging” and “de-pooling” caused by a bill-and-keep regime would certainly make it extremely difficult for the Commission to preserve and advance universal service through specific and predictable support mechanisms – and impossible if the universal service fund (USF) remains capped. The revenue currently recovered through interstate access charges can be recovered from two other sources: (1) end-user charges, and (2) universal service support or some other “cost sharing” mechanism. Thus, under a bill-and-keep regime, in order for rates in rural areas to remain affordable and comparable to those in urban areas, as section 254(b) requires, universal service funding would have to grow.<sup>25</sup> Also, if federal line charges increase under a bill-and-keep regime, Lifeline funding will have to increase, assuming the Commission wants to continue the current program of waiving such charges for low-income customers.

Furthermore, the substantial increases in end-user charges that would result under a bill-and-keep regime would shift a larger portion of USF contributions to LECs. Thus, in addition to higher end-user charges, rural subscribers would also be saddled with higher fees to support the very fund that is intended to offset the higher cost of their local service. In any event, substantial growth in the USF has been a concern for the FCC in the past, and some argue that it is politically unacceptable. If the Commission is unwilling to allow the fund to grow beyond the

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<sup>25</sup> To the extent that bill-and-keep was also instituted by states for intrastate access, the same upward pressures would be placed on state universal service funds.

presently imposed cap, end-user charges and rates in many rural areas will almost certainly become unaffordable and/or incomparable to urban rates, possibly causing subscribers to drop off from the network or to decrease their network usage.

Finally, the NPRM asks for comment on the elasticities of demand with respect to network usage and subscription, in order to assess the extent to which increases in flat-rated charges may affect telephone penetration levels.<sup>26</sup> The Commission appears to be implying that, if most subscribers are willing to remain connected to the network -- despite significantly higher end-user rates -- then implementing a system that has this impact without concurrently adopting a sufficient support mechanism is acceptable. Not only is this burden on rural subscribers unacceptable, but if those higher rates are unaffordable or rural rates or services are not comparable to those being offered in urban areas, it would also be unlawful.

While we do not know exactly what each rural subscriber's rate limit is before he or she drops off the network, we do know that the average household income is more than 20 percent lower in rural carrier service areas than in non-rural carrier areas.<sup>27</sup> This implies that the rate threshold for customers of rural LECs is most likely lower than that of customers of non-rural LECs. Admittedly, it is likely that the overall elasticity of demand for telephone service is low, because most view service as a lifeline and therefore essential to their daily lives. But it is for that very reason that even a small drop in subscriber penetration is unacceptable and entirely inconsistent with the fundamental tenet of universal service first established in the Communications Act of 1934 and further articulated in the 1996 Act.<sup>28</sup> Additionally, those customers that remain connected despite higher rates should not have to make difficult choices

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<sup>26</sup> NPRM at para. 123.

<sup>27</sup> RTF White Paper 2 at pp. 13, 59.

between phone service and other life necessities. Therefore, the Commission should not be approaching the universal service implications of intercarrier compensation reform from the standpoint of how much subscribers are willing to withstand. It should be seeking ways to maintain the same rate affordability and comparability high-cost customers now have, while still providing carriers with the resources to invest in and deploy new and advanced services.

## **V. CONCLUSION**

The Commission has released an NPRM proposing a unified bill-and-keep intercarrier compensation regime, as well as other possible reforms to existing rules. However, this can only be the starting point to what will need to be a comprehensive and lengthy examination into proposals that would have massive and far-ranging impacts on carriers, state and federal authority, and most importantly, consumers. This examination requires the input of all stakeholders, including carriers, the two federal-state joint boards, and individual states. For the rural, ROR-regulated members of NRTA and OPASTCO, the proposals are particularly difficult to assess at this point, as the Commission has yet to adopt an interim access charge reform plan, such as the one under consideration in CC Docket No. 00-256. As the Commission moves forward, it should continue to analyze and consider the way in which its proposals may have different or more severe impacts on uniquely situated rural carriers and their subscribers. Most importantly, this means adopting mechanisms to mitigate the adverse and unlawful universal service and end-user rate impacts *prior* to the adoption of any new regime.

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<sup>28</sup> Congress and the Commission have long recognized that the value of the public switched network is diminished for *all* users when even one subscriber disconnects. This is why Congress, the FCC, and state commissions have successfully pursued policies that promote high subscriber penetration.

Respectfully submitted,

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